

Transitional Exporting: A Case Of Two Emerging Markets

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ABSTRACT

This international business case allows for the evaluation of Eastern European markets and highlights their unique nature. Eastern Bloc countries are newer entrants to the global arena and offer opportunities for understanding an array of emerging markets. The case presents one start-up business and the process, opportunities and roadblocks encountered.

Keywords: International Business; European Union; Entrepreneur; Exports; Embargo; Emerging Markets

INTRODUCTION

Georgia is a nation approximately the size of West Virginia and was part of the former Soviet Union. It is a country that is in the crossroads of many important geographical and political decisions. Turkey borders it along the southern reaches of its countryside, Russia along the north, and the Black Sea on the East. Georgia has a population under five million people and its government is a representative democracy. Although other former Eastern Bloc countries such as Bulgaria have gained entry into the European Union (EU), Georgia, like its closest neighbors, is not an EU member nation.

In early 2004, Beqa, a Georgian man living in the capital of Tbilisi, started an export business as a sole proprietor using \$10,000 (all figures given in US \$) in savings and his home as the business office. Beqa was in his early twenties with little business experience but big plans. He decided to export mineral water, apples, tangerines and wine to Russia. Each of these products had a high demand in Russia and easy availability in Georgia. Georgian wine and mineral water were especially well liked and accepted in Russia with reputations for being of high quality and low price. Very quickly after establishing his home office and business plan however, Beqa realized his limited financial resources required him to focus on only one product for export and he chose mineral water.

THE BUSINESS

The Initial Decision

Beqa chose Russia as his export market for a number of reasons. First, and possibly most important, was the close geographical link between Russia and Georgia. The roads between the two countries were well established and known to him, and the transportation costs would be minimal. Additionally, railroad transfer of products might be possible if his business grew to that volume and the costs would still be reasonable. Secondly, the trade relationship between the two countries was supportive and friendly. Beqa knew the Russian language well and had good personal relationships and friendships with a number of Russian natives. A fourth factor for Beqa was the number of Russian and Georgian friends who ran businesses in Russia. Although none of these friends was involved in directly exporting from Georgia into Russia, he felt their experience, knowledge and willingness to help him establish his business would prove invaluable to his market entry and long term success. Lastly, Beqa considered the size of the Russian market an unbeatable advantage over any other options for export markets bordering Georgia.

Beginning Operations

Initially, operations were simple. Beqa negotiated with both Georgian and Russian friends who were living in Russia. The extent of his business plan was to buy his product from a wholesaler in Georgia, ship the product to a Russian contact, collect a specific price from the Russian contact and buy more product for shipment. He did not have detailed plans or contracts with any retailers or wholesalers. He was confident that the supply of mineral water was not an issue and that he would be able to find someone to sell to on the Russian end. He did not make detailed financial predictions and saw no need for marketing.

Beqa was following the long engrained method of ‘doing business’ in former communist nations. Free market economies and forces were officially allowed since the mid 1990’s. However, most residents in these emerging markets were not familiar with western business practices and plans from either first-hand experience or specific academic or job training. Additionally, banks were not readily loaning money to start-up businesses. Most businesses, like the one under discussion here, are begun by individuals using their own resources to finance initial operations. Thus, Beqa had no need to provide long term projections or financial plans to outside investors or lenders.

Additionally, the use of written and signed contracts was not even considered. Following the previous 40 years of practice, companies basically produced what they could and assumed they would sell what was produced. Contracts were considered to display a lack of trust and friendship and not legally binding anyway. Beqa knew that his supply of mineral water would depend on the wholesaler’s willingness to provide it to him and that the price and availability could change without explanation. He would simply pass those conditions along to the Russian retailers. Beqa was additionally comfortable with these working conditions because he knew that the situation was the same in both countries.

Beqa bought 10,000 bottles of Nabeghlavi Mineral Water in early 2004. The cost per bottle was \$.40, so the total paid was \$4,000. Based on his verbal negotiations, he sent 5,000 bottles each to the Russian cities of Krasnodar and Moscow. He spent \$4,000 to ship via ground transport. The Russian business partners sent Beqa \$1.00 per bottle upon receipt of the shipment

This first shipment went perfectly and was considered a great success from all involved. Thus Beqa continued this process of making phone calls to Russian friends, finding out how many bottles of water they wanted, purchasing the bottles from a plant in Georgia, shipping the mineral water into Russia and accepting payment upon delivery of goods.

Beqa’s export business grew rapidly and he encountered no issues with supply on the Georgian side or demand on the Russian side. He had several new customers in Russia based on word of mouth. The initial contact was always made from the Russian end of the business. An existing customer would tell a friend about his contact in Georgia and they would contact Beqa. Beqa did not seek out additional Russian partners and felt that he was successful enough in allowing them to find him.

After eight months of operation, someone in Russia contacted Beqa and asked if he could begin shipping Georgian wine for their restaurants. He contacted wine makers the next day. It took three months for Beqa to find the right suppliers. He needed someone that could provide a steady supply of good quality wine and with whom he felt he could count on to be honest and fair. Additionally, given that he wanted an initial shipment of 1,000 bottles, he needed to find someone willing to sell that quantity. Most vineyards were capable of producing up to 100,000 bottles per year and did not want to sell such a small percent of their product to Beqa. Vineyards usually sold a quantity of 17,000 bottles minimum per order to protect their cost margin.

Beqa knew that the wine he was shipping to Russia was considered to be moderate in quality. However, demand for Georgian wine was very high in Russia and the first shipment sold very well. Georgian wine was highly demanded in Russia due to being very inexpensive for the Russian consumer.

A Growing Business

Within two years, by April of 2006, Beqa was successfully and regularly shipping mineral water, wine, tangerines and apples to various customers in Russia. He had thirty employees, had moved to a small office space near his home, and made enough money to live comfortably. Additionally, he had replaced the \$10,000 in his savings account. His business was not yet at the point that he could save additional money or afford to invest in real estate, but he was able to live comfortably and pay his employees. He felt that his business was successful and could continue to grow because his contacts in Russia knew that he was reliable and honest.

It was at this point that Beqa became aware of the high demand for parsley in Russia. Friends in Georgia were exporting their supply of parsley to Russia but the process was quite risky due to the highly perishable nature of parsley. Ground transport was not an option for this product. Beqa considered branching out into parsley but was particularly concerned with the need for developing a new and reliable transport method for this one product.

Although air transport was very expensive, Beqa decided to try exporting the parsley. He felt like demand was high enough and some of his Georgian competitors had ruined their own reputation in the Russian market due to providing damaged parsley shipments via ground transport. His first small shipment of parsley went by plane to Krasnodar, Russia.

Embargo

Six months later, in October 2006, Russia set up an embargo that severed all postal and transportation links with Georgia. The Russian government stated that the embargo was due to the arrest and deportation of four Russian military officers accused of spying in Georgia. Most Georgians, Beqa included, believed the motive to be quite different. Georgia was involved with ongoing dialogue with NATO that could cause Georgia to politically and financially distance itself from Russia. The embargo is still in place, five years later.

Decisions

Beqa's business came to an immediate halt. Fortunately, he did not have excessive inventory on hand due to his continued method of buying only what he needed to fill specific orders. Within days of the onset of the embargo, several Russian buyers of his exports called with offers to help smuggle the products into Russia. Some even spoke of their good friends in the government who were willing to assist them. Beqa knew he did not want to become involved in the illegal practices of smuggling, black markets and bribery.

Within a week Beqa would need to release all his employees. He struggled to repay the small amount of debt the business had accrued as well as the immediate bills for the latest purchases that never shipped. Beqa felt particular stress and anger with himself for not pursuing other trading partners in the last two years.

As he struggled to assess the situation, Beqa felt he had three alternatives. First, close the business and sell all assets as quickly as possible to pay off any debt. Second, accept the offers to smuggle goods into Russia and hope the embargo would be lifted quickly. Third, start all over by seeking new markets and acquiring loans from the banks.

CONCLUSION

Beqa felt a strong responsibility for his employees. Although it required several months of rebuilding, he came up with a business plan to allow the company to continue. The plan required a reduction in hours worked and the release of a few employees but within seven months the company was again ready to export.

Although he knew the process would take time, Beqa felt confident he could use the knowledge gained through the last few years of business to expand beyond the comfort zone of the Russian market. However, he also recognized that most anywhere else he exported, the demand would be for a higher quality product than what he was able to ship to Russia. Beqa established business partnerships with other Georgian friends who were willing to

invest small sums of money in order to become part owners in his business. This step was only possible due to his demonstrated success the previous few years. Additionally, the banking environment had progressed to the point that he was able to secure a small business loan to specifically partner with and improve conditions and product quality in a winery.

In April 2007, his company was again ready to export. The first shipment was 200 bottles of wine to Riga, Latvia. Slowly, carefully, they added shipments to Lithuania and Estonia. These markets, as part of the former Soviet Union, offered a customer base that was familiar with products from Georgia and a respect for their wine.

Eventually Beqa's company shipped wine to Sweden and Finland also. Their initial product base, Nabeghlavi mineral water, was shipped to Uzbekistan and Kazakhstan. While sticking to these two products, the company has maintained financial stability and employment. Although current operations are not as wide scale or as profitable as they were with Russia, Beqa takes pride in maintaining his company despite what seemed to be an insurmountable obstacle.

QUESTIONS FOR DISCUSSION

1. Review Beqa's reasons for choosing his export market. Was his evaluation thorough enough? Were there other factors that should have been considered? Which other markets, if any, would have been possible options? Would there have been more advantages or disadvantages for choosing more than one market for the initial entry?
2. Why might the vineyards have been hesitant to sell (all or even some of their product) to Beqa? Do you think the vineyards made a good business decision in selling part of their supply to Beqa?
3. Research the embargo discussed in this case. What is your opinion on pros and cons for the embargo for both the Georgian economy and the Russian economy? What other embargos could you compare it to?
4. Could a more detailed business plan at the outset have changed what happened to Beqa's company?
5. What other options could Beqa have pursued besides closing down his business?
6. What are some of the ethical dilemmas in this case? Are they culturally unique for this market?
7. Discussion topics: political risk, ethics, strategy and planning, the four p's of marketing.

AUTHOR INFORMATION

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Authors' Note: This case is one of six cases in work that relate to the specific markets of Eastern Europe. The idea and hope is to see the cases as viable learning units that can be used individually or as a complete unit of study. The cases deal with countries, issues and economies that receive very little attention in research, textbooks and academic literature. However, with the acceptance of some former communist countries into the European Union, and others seeking application and inclusion, it is imperative that we begin to understand the methods of operation, opportunities and business culture of these emerging markets.